

August 29, 2022

Submitted via email to regs.comments@federalreserve.gov

Ann E. Misback

Secretary of the Board

Board of Governors of the Federal Reserve System

20th Street and Constitution Avenue, NW

Washington, DC 20551

Re: Proposed Rule – 12 CFR Part 253 – Docket No. R-1775 – RIN 7100-AG34;
Regulation Implementing the Adjustable Interest Rate (LIBOR) Act;
87 Federal Register 45,268-45,281 (July 28, 2022)

Dear Ms. Misback:

The Federal Agricultural Mortgage Corporation (Farmer Mac) is pleased to have this opportunity to respond to the request for public comment on the proposed rule (Proposed Rule) of the Board of Governors of the Federal Reserve System (Fed Board) to implement the Adjustable Interest Rate (LIBOR) Act (LIBOR Act) enacted earlier this year. We recognize that an orderly transition away from the benchmark London interbank offered rate (LIBOR) for transactions denominated in U.S. dollars (USD) is a complicated and critical task and appreciate the Fed Board's efforts to help provide a solution for replacing references to USD LIBOR in existing contracts without adequate fallback provisions. This letter provides our observations and suggestions that we believe will enhance the Proposed Rule and help achieve the Fed Board's objectives. Our comments center on two issues: (1) potential ambiguity in the proposed definition of "covered GSE contract"; and (2) the disadvantages of designating multiple benchmark replacements for cash transactions, with Farmer Mac's strong preference being "CME Term SOFR" rather than "30-day Average SOFR" (as both those terms are defined in the Proposed Rule) for all cash transactions.

Background Information About Farmer Mac and Its Transition Away from LIBOR

Farmer Mac is a stockholder-owned, government-sponsored enterprise that combines private capital and public sponsorship to serve a public purpose. Congress has charged Farmer Mac with the mission of providing a secondary market for a variety of eligible loans to help increase the availability and affordability of credit for the benefit of American agriculture and rural communities. The vast majority of loans eligible for Farmer Mac's programs are business-related commercial loans rather than consumer loans. Farmer Mac's secondary market activities include:

- purchasing eligible loans from lenders;
- providing funding to lenders by purchasing securities that are secured by eligible loans; and
- issuing and guaranteeing securities that represent interests in pools of eligible loans.



Farmer Mac funds its purchases of eligible loans and securities primarily by issuing debt obligations of various maturities in the public capital markets. Farmer Mac also uses the proceeds of debt issuance to fund liquidity investments that must comply with applicable regulations of the Farm Credit Administration, which is Farmer Mac's safety and soundness regulator.

Farmer Mac's secondary market functions as a bridge between the public capital markets and the U.S. agricultural and rural credit markets by attracting additional capital sources for financing rural borrowers such as farmers, ranchers, agribusinesses, and rural infrastructure providers of electricity, telecommunications services, and renewable energy. This secondary market is designed to help build a strong and vital rural America by enhancing lenders' ability to offer competitively-priced financing solutions to borrowers through the benefits of capital markets pricing and product innovation. As the nation's secondary market for agricultural and rural infrastructure loans, Farmer Mac does not originate loans to rural borrowers. Instead, we offer a broad array of financial solutions to lenders seeking capital, liquidity, favorable funding, portfolio diversification, or access to a wide variety of loan products in support of their origination efforts. This supports the flow of flexible, low-cost financing to eligible borrowers, which helps drive efficient capital deployment to the agriculture and rural infrastructure sectors.

Farmer Mac has been actively monitoring the financial industry's transition away from USD LIBOR and has been working diligently since 2018 to prepare for the transition to alternative reference rates. Those efforts have included working closely with Farmer Mac's safety and soundness regulator and actively participating in many industry-wide and regulatory advisory committees,¹ all as part of a thoughtful and deliberate process to replace USD LIBOR. During 2018, Farmer Mac discontinued the issuance of LIBOR-based floating rate debt securities with reset dates after the end of 2021 and started issuing floating rate debt securities based on the Secured Overnight Financing Rate (SOFR) in 2019.² Farmer Mac began phasing out its LIBOR-based loan products offered to lenders in 2019 and no longer offered loan products indexed to LIBOR by mid-2020. Since then, Farmer Mac has proactively worked with lenders to discuss alternatives for existing LIBOR-indexed loans held by Farmer Mac. Those efforts include requesting borrowers to convert their existing LIBOR reference rates to another index or to amend loan documentation to provide appropriate fallback provisions. Farmer Mac has made significant progress in those efforts but continues to be involved in legacy transactions whose interest rates reset based on LIBOR. Those transactions include Farmer Mac's ownership of

¹ Farmer Mac representatives have served as members of relevant subcommittees and working groups of the Alternative Reference Rates Committee (ARRC) organized by the Fed Board and the Federal Reserve Bank of New York.

² Farmer Mac had \$1.8 billion outstanding debt securities based on SOFR as of June 30, 2022.

\$3.1 billion of USD LIBOR-based floating rate assets related to Farmer Mac's Agricultural Finance and Rural Infrastructure Finance lines of business and liquidity investment portfolio, out of \$25.9 billion of total assets held as of June 30, 2022.

Potential Ambiguity in the Definition of Covered GSE Contract

The Proposed Rule defines the term "covered GSE contract" as "a covered contract for which a **GSE is identified as a party in the transaction documents and that is (i) a commercial or multifamily mortgage loan**, (ii) a commercial or multifamily mortgage-backed security, (iii) a collateralized mortgage obligation, (iv) a credit risk transfer transaction, or (v) a Federal Home Loan Bank advance." (*Proposed Rule 12 CFR § 253.2; emphasis added*). The commentary in the Proposed Rule about the Fed Board-selected benchmark replacements for "covered GSE contracts" suggests that the Fed Board intended to use that term as a special category of cash transactions that are not consumer loans for one particular reason – to designate 30-day Average SOFR rather than CME Term SOFR for specified cash transactions involving the housing-related GSEs supervised by the Federal Housing Finance Agency to enhance the liquidity of newly issued multifamily loans and other structured products of those GSEs (*see 87 Fed. Reg. 45,276 (July 28, 2022)*). That reasoning does not apply to Farmer Mac, which does not use 30-day Average SOFR in any of its SOFR-based loan products or SOFR-based securities issued in the capital markets. Farmer Mac is concerned that the proposed definition of "covered GSE contract" is broad enough that it could, contrary to the Fed Board's apparent intent to limit the definition to the housing-related GSEs, be interpreted to include the legacy LIBOR-based loans held by Farmer Mac.³

To illustrate, one potential interpretation of the proposed definition is that because Farmer Mac is a GSE⁴ that owns legacy LIBOR-based loans that do not provide for the use of a clearly defined or practicable replacement benchmark rate and that are commercial in nature rather than consumer loans, those legacy loans are "covered GSE contracts" and therefore must use 30-day Average SOFR as the replacement benchmark for LIBOR. Such a requirement would create unnecessary and potentially burdensome challenges for Farmer Mac as it seeks to complete the already-difficult transition away from LIBOR. For example, that requirement would result in a mismatch between the SOFR-based interest rates paid on legacy assets using

³ Farmer Mac considered that perhaps its mere ownership of a loan acquired through a secondary market purchase or assignment would not be deemed as being "identified as a party in the transaction documents" under the definition of "covered GSE contract" because Farmer Mac is not the originating lender on the loans it purchases, but the definition appears to be directed at the activities of the housing GSEs supervised by the Federal Housing Financial Authority, some of which acquire loans through secondary market activities.

⁴ Farmer Mac meets the definition of a "GSE" in the Proposed Rule as "an entity established or chartered by the U.S. government to serve public purposes specified by the U.S. Congress but whose debt obligations are not explicitly guaranteed by the full faith and credit of the U.S. government." (*Proposed Rule 12 CFR § 253.2*).

the proposed replacement benchmark (lagging 30-day average of SOFR rates) and Farmer Mac's SOFR-based funding in the capital markets (daily-average SOFR in arrears), making it more difficult for Farmer Mac to manage interest rate risk on those assets. Given the SOFR rate used by Farmer Mac for funding, interest rates on assets benchmarked to CME Term SOFR are easier to hedge than the proposed 30-day Average SOFR. Farmer Mac would also be faced with the operational challenges of administering SOFR-based floating rate assets and liabilities using several different calculation methodologies – term SOFR for derivatives and Farmer Mac's existing and new SOFR-based loans, daily-average SOFR in arrears for debt funding, and 30-day Average SOFR for the LIBOR legacy assets if required to use the proposed replacement benchmark.

This ambiguity about the intended scope of “covered GSE contracts” could be clarified in a variety of ways to address Farmer Mac's concern. Perhaps the most straightforward way would be to revise the definition of “GSE” in the Proposed Rule to specifically limit it to the entities directly supervised by the Federal Housing Finance Agency.⁵ The Fed Board could also consider adding clarifying language that agricultural and rural infrastructure loans are not considered to be the types of “commercial loans” referenced in the definition of “covered GSE contract” and instead should be classified as cash transactions that are not consumer loans or covered GSE contracts. That treatment would result in the forward-looking CME Term SOFR being the designated benchmark replacement for Farmer Mac's legacy LIBOR-based loans, which is more consistent with Farmer Mac's existing SOFR-based loans and SOFR-based funding compared to 30-day Average SOFR.

The Designation of Multiple Benchmark Replacements for Cash Transactions Could Create Operational Challenges As Well As Confusion and Fragmentation in the Market for Cash Transactions

The Proposed Rule designates two different benchmark replacements for cash transactions. For all cash transactions that are not covered GSE contracts, the Proposed Rule designates CME Term SOFR, a forward-looking term rate, as the benchmark replacement in place of one-, three-, six-, or 12-month tenors of LIBOR.⁶ (*Proposed Rule 12 CFR §§ 253.4(b)(1)(ii), 253.4(b)(2)(i)(B) & 253.4(b)(2)(ii)(B)*). For all covered GSE contracts, the Proposed Rule designates 30-day Average SOFR, a lagging 30-calendar-day compounded average of SOFR, as the benchmark replacement in place of one-, three-, six-, or 12-month tenors of LIBOR. (*Proposed Rule 12 CFR*

⁵ It should be noted that this potential solution could create some confusion among the Fed Board's regulated institutions with the existing definition of “GSE” used in the Fed Board's capital rule (12 CFR § 217.2), which was the model for the definition of “GSE” in the Proposed Rule.

⁶ As required by the LIBOR Act, interest rates on consumer loans will be determined using a modified tenor spread adjustment for the first year after the LIBOR replacement date, but the benchmark SOFR rate is the same for consumer loans and all other cash transactions that are not covered GSE contracts (CME Term SOFR).

§ 253.4(b)(3)(ii)). Besides the potential funding mismatches and operational challenges discussed in the section above, the designation of two different benchmark replacements for cash transactions does not appear to be consistent with one of the LIBOR Act's primary purposes of providing a uniform solution for replacing LIBOR in what the Fed Board has described as "tough legacy contracts."

A different benchmark replacement for covered GSE contracts compared to other cash transactions is not required by (or even mentioned as a possibility in) the LIBOR Act. Designating a different benchmark replacement for covered GSE contracts could create unnecessary confusion and fragmentation in the market for cash products. Also, such an approach would affect not only the operations of the in-scope GSEs – it also could have significant ramifications for any participants in the capital markets who purchase the affected securities of those GSEs but who use other SOFR rates for other aspects of their operations. Applying a lagging 30-day Average SOFR alternative reference rate could also create volatility in earnings during periods of frequent or significant changes in short-term interest rates due to monetary policy activity or lead to ineffectiveness of hedges for some institutions.

Farmer Mac has worked closely with the ARRC during the last four years to provide input about the appropriate approach to LIBOR fallback language. We agree with the ARRC's guiding principles to adopt similar fallback language for cash products and the ARRC's recommendations to use CME Term SOFR as the primary replacement rate for USD LIBOR in those products. We believe that forward-looking term SOFR rates, after adding the appropriate adjustment spreads, are the closest economically to the LIBOR benchmark rates being replaced in legacy covered contracts. Term SOFR rates are also likely the simplest choice to replace USD LIBOR for most participants in the non-derivative markets. We encourage the Fed Board to adopt a coordinated approach to fallback language across all cash market products to promote a successful transition from USD LIBOR to alternative reference rates. We believe that the holders and issuers of these covered contracts would benefit if the Fed Board's final rule designated the forward-looking CME Term SOFR indexes as the SOFR-based benchmark replacement for all cash transactions rather than designating the lagging 30-day Average SOFR benchmark for a separate subset of cash transactions.

We thank you for the opportunity to comment on the Proposed Rule.

Sincerely,



Aparna Ramesh
Executive Vice President – Chief Financial Officer